USAID | IRAQ

FROM THE AMERICAN PEOPLE

AGRICULTURAL POLICY DIALOGUE SERIES #9

Strengthening Agricultural Input Supply Services in Iraq

January, 2011

This publication was produced for review by the United States Agency for International Development.
It was prepared by USAID-*Inma* Agribusiness team for a consortium led by The Louis Berger Group, Inc.

AGRICULTURAL POLICY DIALOGUE SERIES #9

Strengthening Agricultural Input Supply Services in Iraq

DISCLAIMER

Table of Contents

Strengthening Agricultural Input Supply Services in Iraq .... - 1 -
Current Status .... - 1 -
A Strategy to Strengthen the Agricultural Input Supply (AIS) System .... - 2 -
An “Open Franchise Business Model” for Agricultural Input Supply........................ - 3 -

Strengthening Agricultural Input Supply Services in Iraq

This paper proposes an option for transitioning from the state dominated agricultural input supply system in Iraq to a vertically integrated private sector owned and operated system.

Current Status

Until the 2003 conflict, a considerable network of inter-related state-owned companies dominated input supply markets[1], including retail sale and distribution, and, especially for certain "strategic" crops, at highly subsidized prices.

With the collapse of the Saddam regime and subsequent increases in sectarian and criminal violence, most state-owned companies greatly reduced or ceased operations. Nevertheless, much of the infrastructure and personnel of these companies remained in place. Additionally, over the past two years, considerable donor funds have been invested in rehabilitation of state-owned agriculture-related companies, and recently, a number of state-owned agricultural input supply, processing and marketing companies, have been receiving increased Government of Iraq (GoI) funded operating budgets to again actively dominate both wholesale and retail agricultural input supply operations.

During the period of disarray in state-owned company operations following the 2003 conflict, private sector entrepreneurs began to fill the void. And there have been efforts by donors and local governments to organize producer groups into business enterprises to supply inputs and other services to members. Nevertheless, both wholesale and retail levels of the marketing system for agricultural inputs remain rather chaotic, poorly organized, and largely dysfunctional. Most state-owned and private sector input supply enterprises are under-capitalized and have limited management capabilities. These enterprises generally must directly import or make arrangements with an agent to import input supplies, i.e., there is no organized wholesaling structure to serve input supply retailers. Or they are "resellers" of inputs from farmers who re-sell their allocations from state-owned companies.

Uncertainty about the future role of state-owned enterprises in agricultural input supply (often at subsidized prices) discourages private entrepreneurs from making

[1] State Company for Agricultural Supplies (SCAS), State Company for Industrial Crops (SCIC), Mesopotamia and State Seed Companies, State Veterinary Services Company, among others. Other companies manufactured inputs, marketed output or performed other agriculture-related services.

greater commitments to input supply business development, either at wholesale or retail levels. Several state-owned companies are now receiving budget resources that permit them to produce (or import) and distribute fertilizers and other chemical inputs at subsidized prices.

A Strategy to Strengthen the Agricultural Input Supply (AIS) System

Development of a comprehensive strategy to strengthen the AIS system in Iraq should consider the following points:

1. GoI Planning Documents Endorse the Concept of Transitioning to a Market-Oriented Private Sector-Led AIS System. Nevertheless, in practice, the government is re-activating several state-owned agricultural input supply companies (along with other state-owned agriculture-related companies). If Iraq is to achieve a market-oriented, private sector-led AIS system, the GoI urgently needs to develop and commit to a firm "transitioning" strategy.
2. Lessons Learned in Iraq and Elsewhere indicate that the state is a very inefficient retailer of agricultural inputs, and seldom is efficient in other input supply business activities and services. Additionally, public sector direct participation, especially at retail, inevitably distorts markets at all levels of the supply chain.
3. Existing State-Owned Companies in Iraq Hold Considerable Capital Infrastructure and Human Resource Assets. To the extent possible, these assets should be incorporated (and rehabilitated as required) into a future market-oriented private sector dominated AIS system.
4. Emerging Private Sector Input Suppliers at Retail level Often Lack Financial Resources, Management Capabilities and/or Business Know-How required to plan and develop dynamic and expanding business enterprises.[2] Many treat input supply activities as short-term spot-market trading opportunities. Similarly, due to uncertainties and perceived risks, private sector input supply wholesale operations are weak and underdeveloped, or non-existent.
5. Input Supply Wholesale and Retail Functions Are Distinct Business Specialties with Different Business and Risk Management Parameters. Nevertheless, effective vertical integration of wholesale and retail functions leads to more compatible planning and decision-making throughout the agricultural supply chain, resulting in reduced transaction costs.
6. Retail AIS Businesses Better Serve Producers When They Offer a Full Range of Inputs and Related Services Required by Farmers (one-stop shopping), based on what the farmer produces. In this manner, retail business transaction efficiencies

[2] There are exceptions. For example, at least two private companies supply vegetable producers around Baghdad with imported certified seed and other inputs.

are achieved through specialization by type of farming served, rather than by type of input supplied.

An "Open Franchise Business Model" for Agricultural Input Supply

An open franchise business model is suggested as a practical framework for strengthening the AIS system in Iraq. This approach can accommodate to the points listed above. More importantly, it is an efficient way to achieve vertical integration that strengthens transactional linkages along the entire agricultural input supply value chain, and facilitates forward and backward business information flows for improved decision-making and management. Characteristics of a franchise business model adapted to the Iraqi agricultural input supply system might include:

1. The franchisor business will offer (at wholesale) a comprehensive range of goods and services to private sector franchisees for retailing to producers; the range offered will be responsive to the marketing concept of one-stop shopping.
2. Appropriate state-owned AIS-related companies (one or more) would be restructured to become wholesale input supply services businesses (franchisor) serving multiple input supply retailers (franchisees), eventually expanding franchises to all commercial agricultural production areas in Iraq.
3. Existing or proposed retail AIS enterprises are (or will be) private sector entrepreneurs or producer-owned groups organized as input supply business enterprises. "Company-owned" start-ups may be required in some instances, but should have a time-phased plan for private sector take-over.
4. Input supply enterprises will be selected to become franchisees, based on growth opportunities both in terms of potential service area and business development (intensification) prospects. In order to encourage business competition at the retail level, franchises likely would not be offered on the basis of exclusivity in a defined market area.
5. A variety of agricultural input supply related goods and services will be offered by the franchisor to franchisees for onward retailing to producer clientele, as well as for franchisee internal business operations development and improvement purposes.
6. Depending on the kind and scope of assets directly controlled by the restructured franchisor, goods and services will be offered to franchisees directly or through arrangements with other providers of appropriate goods and services.
7. Goods and services offered or facilitated by the franchisor to franchisees for onward retailing to clientele would include a full range of cash (and capital)

inputs as appropriate for actual and potential clientele of the franchisee. Business activities also would include arranging for or facilitating access to supporting services for producers, such as technical assistance (related both to production technology/best practices and to farm management), market information and advice, credit services, services related to market promotion and facilitating access to active and emerging markets, etc.

8. The franchisor also will provide to franchisees (directly or indirectly through contractors) technical assistance, training and/or services related to improving franchisee business operations and management (may include accounting and record-keeping training and services, business management training and support, personnel skills training, facilitating access to credit, facilitating access to venture capital, etc.).
9. Consistent with the goal of a market-oriented AIS system, all physical inputs wholesaled to franchisees will be transacted at wholesale prices intended to recuperate costs. This may require a "phase-out" period for some inputs that currently are subsidized by the GoI. The competitive edge gained through the franchising arrangement is that the resulting economies of scale and vertical integration efficiencies of wholesale transactions (including warehousing and transport) reduce transaction costs, thus permitting lower wholesale prices as compared to open-market (non-franchise) transactions.
10. During start-up of a particular franchisor-franchisee agreement, supporting services both directly to the franchisee business and through the franchisee to its clients likely would be provided at less than cost (perhaps initially at nominal cost) until franchisee operations are on a trajectory to profitability. Un-reimbursed costs of providing "soft" inputs to the franchisor during start-up would be offset with GoI transfers to the franchisor for a previously agreed-upon phase-out period.
11. Because of the "brain-drain" of Iraq over the past three decades (during Saddam oppression and post-Saddam terrorism), franchisor restructuring design and implementation, as well as long term management of franchisor operations should be contracted through an international solicitation.
12. A mandatory plan would be put in place as a part of restructuring to privatize the franchisor. One option to consider: institute a "check-off" fee system for goods (physical inputs) wholesaled to franchisees. This check-off would become part of the capital base of the franchisor. When the check-off capital reaches a previously agreed share of total franchisor capitalization (perhaps 10-20%), the GoI would transfer ownership or at least management control (through issuance of common shares) to the franchisees.